

RENTAL DEVELOPMENT RESERVE REQUIREMENTS

The following reserve accounts are required by CalHFA on or before permanent loan closing. The accounts are funded with cash or securities acceptable to CalHFA, and remain under the control of the Agency at all times. Any income earned will accrue to the account. Any remaining balance will be returned to the Borrower once all applicable conditions have been met.

- a. **Marketing Account:** A Marketing Account ("MA") is funded in an amount established by CalHFA and maintained until all expenses for which the Account was designated have been paid. The MA cannot be funded with CalHFA loan proceeds and may be used to pay for non-construction items necessary to make the Development operational.

The MA is generally calculated at 10% of the projects gross income. Allowable expenses include:

- Advertising
- Office expenses
- Marketing staff payroll
- Model apartment and common area furniture
- Maintenance tools and equipment
- First year hazard insurance premiums
- Estimated property tax impound adjustments

At permanent loan closing, CalHFA may approve a reduction in the amount of this account for certain MA expense items which have already been paid.

- b. **Rent-Up Account:** A Rent-Up Account ("RUA") is required to supplement operating income during the initial rent-up period. The RUA is established in an amount equal to fifteen percent (15%) of the projected annual gross rental income of the Project.

The RUA cannot be funded with CalHFA loan proceeds. The RUA account will be used to fund any shortfall in rental income occurring between initial occupancy and Sustained Occupancy. "Sustained Occupancy" is achieved when, for at least three consecutive months:

- At least ninety-five (95%) of the total number of units are occupied, and
- Income equals or exceeds that projected on the Final Loan Commitment assumptions, and
- The operating deficit equals or is less than projected on the Final Loan Commitment assumptions.

Monthly disbursements from this account shall be applied first to principal and interest payments on the CalHFA loan, then to required reserves, impound and escrow accounts, and then to other operating expense payments.

The RUA may be released at CalHFA's discretion when Sustained Occupancy is achieved, provided that the Operating Expense Reserve (described below) is fully funded and the Agency has received a copy of all first year Tenant Income Certifications.

- c. **Operating Expense Reserve:** An Operating Expense Reserve ("OER") account is used to fund any operating expenses not covered by gross income, the Marketing Account or Rent-Up Account. The OER account must be established and maintained from sources other than development income in an amount equal to the greater of:

- Ten percent (10%) of the projected initial annual gross rental income, or
- An amount fixed by CalHFA on a per loan basis

The OER may be released after two full consecutive project fiscal years have passed in which the annual audited financial statement accepted by CalHFA shows that the project operations generated surplus cash.

- d. **Replacement Reserve:** A Replacement Reserve account ("RR") is used to fund extraordinary maintenance or repair, replace major structural elements or equipment of the Project, or for any other purpose consistent with maintaining the financial and physical integrity of the Project. The RR for the Acquisition/Rehabilitation Project shall be funded in an amount based on a Physical Needs Assessment ("PNA") and the Agency's evaluation of the project's capital requirements over the term of the loan. The RR shall be maintained until the termination of the Regulatory Agreement.

Each year that the Regulatory Agreement is in effect, the amount of the RR is paid in twelve equal monthly installments along with payments of principal, interest and taxes. CalHFA may increase the required RR deposits at any time that it deems necessary. Any balance remaining in the RR when the Regulatory Agreement is terminated will be returned to the Borrower.

- e. **Construction Defects Escrow:** A Construction Defects Escrow Account ("CDE") is required to cover any latent defects in construction. The CDE account is generally established in an amount equal to two and one half percent (2.5%) of the hard construction costs for twelve months from the date of the permanent loan closing. The CDE is in the form of cash or a letter of credit acceptable to CalHFA.